

Memorandum

TO: HONORABLE MAYOR AND
CITY COUNCIL

FROM: Larry D. Lisenbee

**SUBJECT: MONTHLY FINANCIAL REPORT
FOR AUGUST 2003**

DATE: October 21, 2003

Approved

Date

INFORMATION ONLY

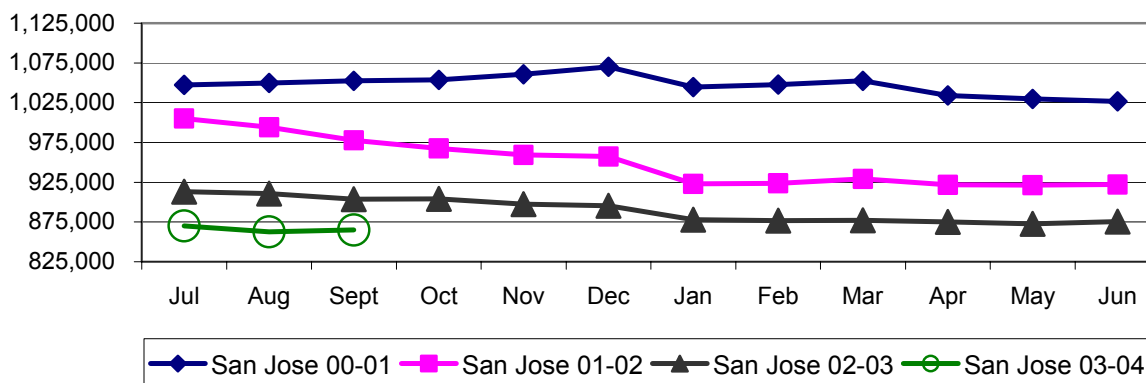
The Monthly Financial Report (MFR) for August was jointly prepared by the City Manager's Budget Office and the Finance Department and is presented here for the City Council's review.

OVERVIEW

A review of the financial status of the City through the first two months of the fiscal year, although based on very limited data, serves to confirm that the City continues to be negatively impacted by the severe slowdown in the local economy. Although the regions's economic situation appears to have stabilized, there are as yet no real signs of recovery.

The most crucial indicator of economic health in our view continues to be the employment situation in the County, and regrettably, job losses still plague our economy (see chart below).

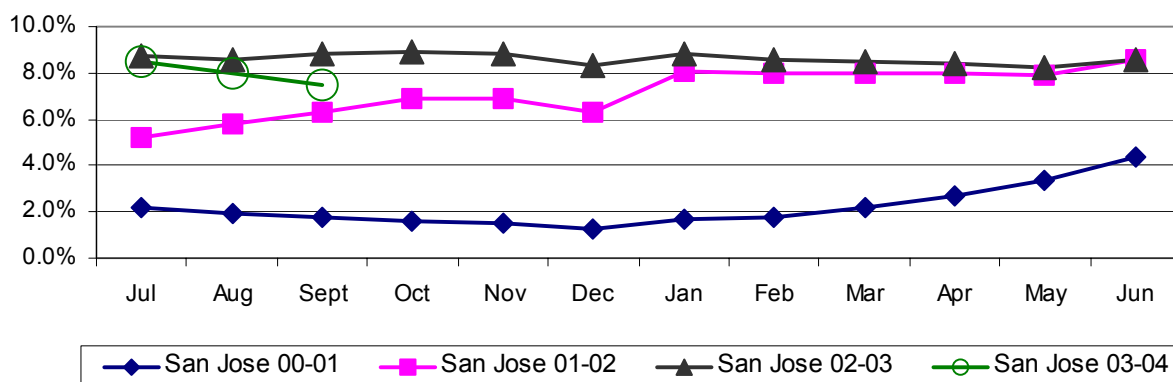
San José Metropolitan Statistical Area
(Santa Clara County)
Employment: Total Jobs Comparison



OVERVIEW (CONT'D.)

September employment information was released last week, and on the surface, the numbers seem positive. The unemployment rate of 7.5% was down from August's adjusted rate of 8%, and the number of unemployed residents fell, from 74,200 to 67,800. Upon closer review, however, it is clear that these statistics masked the real situation, because the most important indicator, the number of jobs in the County, dropped again, by 2,300, from 867,100 to 864,800. Thus, the drop in the unemployment rate and the number of unemployed were in reality the result of jobless residents leaving the County or leaving the workforce. The 864,800 jobs represented the lowest job level reported since February 1996. The County unemployment rate through September also remained well above both the state and national rates, which were 6.1% and 5.8%, respectively.

San José Metropolitan Statistical Area
(Santa Clara County)
Unemployment Rate Comparison



The state of the economy continues to directly affect collections of the economically sensitive revenues. The most dramatic illustration of this negative impact remains the General Fund's largest single revenue source, Sales Tax. The City recently received its latest General Sales Tax information (representing the final quarter of the 2002-2003 fiscal year) and the news was again disappointing. While not reflected in the August numbers shown in this report, the September final Quarterly Sales Tax reconciliation (representing economic activity in April, May and June) was down 1.4% from the same quarter in the prior year. This was the ninth consecutive quarter in which City Sales Tax collections declined. Though the drop was not as great as the previous quarters, the news was still discouraging, particularly because the drop was from a poor prior year quarter that had itself been down by 16.7% from the 2000-2001 level. It should be noted, however, that the Administration had anticipated the weak performance by building a conservative 10.0% drop into the 2002-2003 fourth quarter accrual estimate. This actually allows the City to begin the new fiscal year with a small cushion in Sales Tax revenue. This collection level was, however, slightly below the level anticipated when the 2003-2004 estimate was constructed.

On an overall basis, the first two months of the year were characterized by continuing weakness in key economically sensitive revenues. In addition, as described below, unanticipated problems in two key revenue sources, Motor Vehicle License Fees and Electricity Utility Taxes, will result

OVERVIEW (CONT'D.)

in reduced collections of approximately \$2.4 million. Despite that fact, however, while noting how little data has been received to date, we believe that collections can still be described as performing within budgeted expectations. The Council will of course be continuously updated on the status of our monitoring through these MFR reports as the year progresses.

It should also be noted that in response to the continued weak economic performance, and in light of the projections for major budgetary shortfalls to face the City next year, the Administration is continuing to implement the aggressive cost control strategies that have been in place for over a year. A city-wide hiring freeze continues to be in effect, as well as the freezes on various non-essential expenditure categories (e.g., overtime, travel, large equipment purchases, marketing, etc.). In addition, departments are currently in the process of drafting Cost/Position Management Plans for the 2003-2004 fiscal year.

GENERAL FUND

Revenue Collections

General Fund revenues through August 2003 totaled \$91.3 million. This was an increase of \$12.9 million (16.5%) from the August 2002 level of \$78.4 million. This performance was primarily driven by growth in the Transfers and Reimbursements category (\$13.8 million or 54.7%) along with increases in the following revenue categories: Property Tax, Transient Occupancy Tax, Utility Tax, Licenses and Permits, Departmental Charges, and Other Revenue. Growth in those categories was partially offset by decreases in the following revenue categories: Sales Tax, Franchise Fees, Use of Money and Property, Revenue from Local Agencies, and Revenue from the State of California.

The following discussion highlights General Fund activities through August:

KEY GENERAL FUND REVENUES (\$000's)

<u>Revenue</u>	<u>2003-2004</u> <u>Estimate</u>	<u>YTD</u> <u>Actual</u>
Property Tax	\$ 92,438	\$ 959

Year-to-date Property Tax revenues primarily reflect collections in the smallest property tax category, SB 813 Property Taxes (supplemental taxes). Accrual reversals for this revenue category were not recorded until after the August month-end close, resulting in payments of \$825,000 for August. When adjusted for accrual reversals, however, the adjusted total for the current fiscal year through August is \$213,000, which is 17.3% lower than last year's comparable collections of \$249,000. Revenue in this category, representing payments for taxes owed on recent housing resales, are typically a leading indicator of a drop in sales activities.

GENERAL FUND (CONT'D.)

REVENUES (CONT'D.)

Consistent with previous years, no payments for Secured Property Taxes have been received through August. Initial data from the County of Santa Clara indicates growth is currently at or above the expected level for 2002-2003. Staff is working with the County to confirm the preliminary information.

KEY GENERAL FUND REVENUES
((\$000's) (Cont'd.)

<u>Revenue</u>	<u>2003-2004</u> <u>Estimate</u>	<u>YTD</u> <u>Actual</u>
Sales Tax	\$ 128,818	\$ 1,537

General Sales Tax receipts for August represent only State formula advance payments. Collections of \$1.5 million tracked 74.4% lower than the \$6.0 million collection in the prior year. Because these are advance payments, however, the decline through August is not necessarily indicative of an actual drop in receipts.

In fact, although not reflected in this report, the City has now received the most recent quarterly Sales Tax report from the State. As discussed above, and as reported in the 2002-2003 Annual Report, the City's collections levels continue to be weak, with a 1.4% decline from the same quarter last year, and represents our ninth consecutive quarterly decline in Sales Tax receipts. San Jose's decline was less than that experienced by the San Francisco Bay Area (down 2.3%) while the State as a whole actually grew (5.0%). The South Bay regional economy clearly continues to be the hardest hit area in the State, if not the nation. Although our decline is no longer in double digits it is still obvious that a weakened economy, and a resultant decline in Sales Tax collections, continues.

Preliminary information from MBIA MuniServices, the City's Sales Tax consultants, indicates that the decline in the City's Sales Tax receipts for the most recent quarter can be attributed to poor performance in most economic sectors, but was led again, not surprisingly, by a yet another decline in the Business-to-Business category (down 7.6%). The following categories also suffered significant drops: Transportation (down 6.3%); Construction (down 5.4%); and Food Products (down 3.9%). Within the Business-to-Business category, the greatest declines were related to leasing (down 26.7%), office equipment (down 11.6%), heavy industry (down 9.9%), and electronic equipment (down 5.2%). Within the Transportation sector, the greatest decline was in service stations (down 11.2%) and new auto sales (down 4.8%). The following lists the largest General Sales Tax sectors and their percentage of the total for the 2002-2003 fourth quarter (March through June economic activity): Business-to-Business at 27.5%; General Retail at 25.9%; Transportation at 22.0%; Food Products 13.4%; and Construction at 10.2%.

GENERAL FUND (CONT'D.)

REVENUES (CONT'D.)

KEY GENERAL FUND REVENUES
(\$000's) (Cont'd.)

<u>Revenue</u>	2003-2004 <u>Estimate</u>	YTD <u>Actual</u>
Transient Occupancy Tax	\$ 6,719	\$ 322

Transient Occupancy Tax (TOT) collections through August of \$322,000 were above last year's level of \$182,000 for the same period. This increase was, however, almost entirely due to the impact of prior year accruals. After accounting for those accruals, TOT receipts were actually down by 6.0% compared to the prior year.

The August 2003 occupancy rate in the largest hotels was 53.2%, up slightly from the August 2002 rate of 53.1%, but below the July 2003 rate of 56.8%. It should be noted, however, that although the number of rentable rooms remained relatively stable, the average room rate continued to drop, from \$100.37 from \$120.05.

<u>Revenue</u>	2003-2004 <u>Estimate</u>	YTD <u>Actual</u>
Franchise Fees	\$ 32,406	\$ 4,512

Collections of \$4.5 million from Franchise Fees were below the August 2002 collection level of \$4.9 million. This negative variance reflects net lower collections in Electric and Gas Franchise Fees and slightly lower than anticipated collections from City Generated Tow Franchise Fees. The receipts related to Electric and Gas Franchises Fees are the result of formula-driven estimated payments from Pacific Gas & Electric (PG&E), based on actual collections in 2002, and are not necessarily indicative of actual expected receipts. In addition, as reported to City Council in June 2003, net receipts also reflect the repayment of \$183,236 to PG&E for overpayments made to the City in 2002-2003. In April 2004, PG&E will calculate the actual Franchise Fees due in 2003-2004 based on calendar year 2003 activity. The performance related to City Generated Tow Franchise Fees is primarily driven by accrual reversals that were not recorded until after the August month-end close. City Generated Tow Franchise Fees are anticipated to meet budgeted expectations.

Commercial Solid Waste Franchise Fees of \$431,000 were significantly higher than the prior year level of \$280,000. This apparent positive performance was, however, entirely due to the timing and booking of payments by the haulers, that were not recorded until after the August month-end close, and not necessarily indicative of actual expected receipts. After accounting for

the accruals, it appears that this revenue category is down by 4.4%. Preliminary discussions indicate that this performance is primarily due the continued economic climate as well as to

GENERAL FUND (CONT'D.)

REVENUES (CONT'D.)

KEY GENERAL FUND REVENUES

(\$000's) (Cont'd.)

<u>Revenue</u>	2003-2004 <u>Estimate</u>	YTD <u>Actual</u>
Franchise Fees (Cont'd.)	\$ 32,406	\$ 4,512

commercial diversion programs. Though it is still early in the year, preliminary estimates indicate that this revenue category may not meet budgeted expectations. The Budget Office will continue to work with the Environmental Services Department to analyze current year performance and assess whether a downward adjustment should be recommended.

<u>Revenue</u>	2003-2004 <u>Estimate</u>	YTD <u>Actual</u>
Utility Tax	\$ 66,979	\$ 7,458

Utility Tax collections of \$7.5 million are 17.1% above last year's level of \$6.4 million. This apparent increase, however, was driven entirely by accruals for the prior year. Adjusting for this accrual, performance in this category was essentially flat compared to the prior year. Although too early in the year to make definitive projections, collections are running behind expectations in three of the four sources in this category (Electricity, Water and Telephone). Collections of Gas utility tax revenues appear on track. The lower than anticipated collections in the Water and Telephone Utility Tax areas appear to reflect economic activity drops. The projection for a shortfall in the Electricity Utility Tax is the result of a recent announcement by the California Public Utilities Commission that it ordered a one-time rebate to PGE customers. The unanticipated negative impact of that rebate on the City is projected at approximately \$1.1 million. It is likely that a downward adjustment to this revenue category will be required at mid-year.

GENERAL FUND (CONT'D.)

REVENUES (CONT'D.)

KEY GENERAL FUND REVENUES
(\$000's) (Cont'd.)

<u>Revenue</u>	<u>2003-2004</u> <u>Estimate</u>	<u>YTD</u> <u>Actual</u>
Licenses and Permits	\$ 66,743	\$ 12,233

On an overall basis Licenses and Permits revenue of \$12.2 million through August was 17.0% above the prior year level.

Cardroom Business Tax collections of \$679,000 were well above the prior year level of \$292,000. This performance was primarily driven by the Bay 101 bankruptcy filed at the same point last year where revenue was not received during that period. This revenue category is expected to meet budgeted expectations.

Disposal Facility Tax revenue of \$1.2 million was about flat compared to the prior year level. However, taking into account prior year accruals, this revenue category actually experienced slight growth of 2.5%. Throughout last year, this revenue's weaker performance was driven in large part by market reactions to the removal of the Alternate Daily Cover exemption. Apparently, a portion of the yard trimmings that typically went to City landfills in the past has been transported to other locations (e.g., biomass facilities for energy production). This market reaction seems to be leveling off, stabilizing in the past few months. The Budget Office will continue to work with the Environmental Services Department to analyze current year performance and assess whether a downward adjustment should be recommended.

Fire Permit revenues of \$1.1 million tracked below anticipated levels through August. These fees will continue to be closely monitored and adjustments to the budgeted estimate recommended if indicated as more information becomes available.

Building Permit revenues of \$14.4 million, in contrast, are tracking well above both the budgeted level (15.5%) and last year's collection level (24.3%). Revenues through August collected in all categories performed at or above anticipated levels except for new residential building plan check and mechanical permits.

GENERAL FUND (CONT'D.)

REVENUES (CONT'D.)

KEY GENERAL FUND REVENUES
(\$000's) (Cont'd.)

<u>Revenue</u>	<u>2003-2004</u> <u>Estimate</u>	<u>YTD</u> <u>Actual</u>
Use of Money and Property	\$ 9,733	\$ 469

As anticipated, the Use of Money and Property revenue of \$469,000 was significantly below the prior year level of \$788,000, reflecting lower cash balances and interest earnings. The General Fund cash balance for August was down to \$175.3 million, as compared to the prior year's \$207.2 million, a decline of 18.1% or \$31.8 million. This level was below that assumed in the Adopted Budget, and causes concern regarding the ability to achieve budgeted revenue levels. Continued close monitoring will be required in this category.

<u>Revenue</u>	<u>2003-2004</u> <u>Estimate</u>	<u>YTD</u> <u>Actual</u>
Revenue from Local Agencies	\$ 39,521	\$ 11,884

Revenue from Local Agencies of \$11.9 million through August was 3.6% below the prior year level of \$12.3 million. This variance was primarily driven by several earlier than anticipated payments received in the prior year that were not received early in the current year: Animal Services payments from other agencies (\$176,000), Community Based Aftercare Program funding from the County (\$311,000), and reimbursement for staffing from the Redevelopment Agency (\$530,000). No change in the budgeted revenue estimate is currently believed to be necessary.

<u>Revenue</u>	<u>2003-2004</u> <u>Estimate</u>	<u>YTD</u> <u>Actual</u>
Revenue from the State of California	\$ 58,249	\$ 786

Revenue from the State of California through August totaled only \$786,000, which represented a significant decline from the prior year collection level of \$3.5 million. The drop reflects the impact of the one-time reduction in Motor Vehicle In-Lieu Fee (MVLF) payments included as part of the State budget balancing actions. (As a reminder, that one-time impact results from the ramp-up time necessary to fully implement the increase in the MVLF fees included in the State budget balancing package). Actions approved by City Council in September to revise this

GENERAL FUND (CONT'D.)

REVENUES (CONT'D.)

KEY GENERAL FUND REVENUES
(\$000's) (Cont'd.)

<u>Revenue</u>	2003-2004 <u>Estimate</u>	YTD <u>Actual</u>
Revenue from the State of California (Cont'd.)	\$ 58,249	\$ 786

estimate (a \$10.5 million decrease to the MVLF category) will not be reflected in this report until September. Subsequent to the September re-balancing actions, however, it has been determined that a key assumption used to estimate prior year revenues in this category was in error. Based on statements from the State Controller, the Finance Department presumed that a MVLF payment in the amount of \$1.3 million due to the City in June would be delayed, but eventually paid. An accrual in that amount was, as a result, included in the final 2002-2003 closing statements. We have now learned that this payment will not be forthcoming. The result is shortfall of \$1.3 million in current year collection totals. A downward adjustment in the budget will be required to reflect this accrual error, which will be recommended as part of the Mid-Year Budget Review.

<u>Revenue</u>	2003-2004 <u>Estimate</u>	YTD <u>Actual</u>
Departmental Charges		
-Public Works	\$ 6,405	\$ 1,065

Public Works August revenues of \$1.1 million were 45.8% above the prior year level, but slightly below anticipated levels. As with other revenue categories, this seemingly strong performance over the prior year was almost entirely driven by accrual reversals that were not recorded until after the August month-end close. The three poorest performing categories were residential engineering, private streets engineering and inspection, as well as water quality runoff. Performances in these areas were partially offset by higher than anticipated collections in the non-residential materials testing, non-residential engineering, and planned development prezonings/rezonings categories. While revenues trailed anticipated levels, it is still relatively early in the year. The Budget Office will continue to work with the Department to project the year-end collection level, bringing forward appropriate adjustments if necessary as more information becomes available.

GENERAL FUND (CONT'D.)

REVENUES (CONT'D.)

KEY GENERAL FUND REVENUES
(\$000's) (Cont'd.)

<u>Revenue</u>	<u>2003-2004 Estimate</u>	<u>YTD Actual</u>
Departmental Charges (Cont'd.)		
-Planning, Building, & Code Enforcement	\$ 5,129	\$ 629

Planning Permit revenue of \$629,000 although 9.2% above last year's collection level at this point in time, was running below anticipated levels. Revenue activity for 2003-2004 assumed the same level of activity as 2002-2003, with increases of 15.0% as approved by the Council. Activity levels and collections through August are down, and create some concern regarding the ability to achieve the current budgeted estimate. The Budget Office will continue to work with the Department to project the year-end collection level, bringing forward appropriate adjustments if necessary as more information becomes available.

<u>Revenue</u>	<u>2003-2004 Estimate</u>	<u>YTD Actual</u>
-Parks, Recreation, and Neighborhood Services	\$ 7,177	\$ 2,719

Parks, Recreation, and Neighborhood Services (PRNS) revenues of \$2.7 million tracked significantly above the prior year level of \$1.3 million. This increase reflected primarily, however, accrual reversals that were not recorded until after the August month-end close. After accounting for the accruals through September, PRNS-related revenue is about flat compared to the prior year. It is currently anticipated, however, that this category will end the year at budget.

<u>Revenue</u>	<u>2003-2004 Estimate</u>	<u>YTD Actual</u>
Other Revenue	\$ 12,195	\$ 5,163

Other Revenue collections of \$5.2 million were \$1.5 million above the prior year level of \$3.7 million. This increase from the prior year primarily reflects a planned increase in reimbursement from the Arena Authority. Overall collections appear to be within budgeted expectations.

GENERAL FUND (CONT'D.)

REVENUES (CONT'D.)

KEY GENERAL FUND REVENUES
(\$000's) (Cont'd.)

<u>Revenue</u>	<u>2003-2004</u> <u>Estimate</u>	<u>YTD</u> <u>Actual</u>
Transfers and Reimbursements	\$ 86,035	\$ 38,923

Transfers and Reimbursement collections of \$38.9 million were significantly above the prior year level of \$25.2 million. This performance through August was primarily driven by various transfers to the General Fund, including the Healthy Neighborhood Venture Fund (\$10.0 million) and the Vehicle Maintenance and Operations Fund (\$2.9 million). Overall collections appear to be within budgeted expectations.

EXPENDITURES

Through August, General Fund expenditures of \$96.3 million were 6.3% below (down \$6.6 million) the prior year level of \$102.9 million. Encumbrances of \$49.5 million were 31.8% below (down \$23.1 million) the prior year level of \$72.6 million. Expenditures and encumbrances (\$145.8 million) through August constitute 20.5% of the total 2003-2004 revised, budgeted use of funds (\$709.6 million, excluding reserves).

On an overall basis, cumulative departmental and non-departmental expenditures appear to be within or below approved budgeted levels through August.

The following discussion highlights General Fund expenditure issues:

KEY GENERAL FUND EXPENDITURES
(\$000's)

<u>Department</u>	<u>2002-2003</u> <u>Budget</u>	<u>YTD</u> <u>Actual</u>
Police	\$ 217,776	\$ 29,029

Overall, the Police Department expenditures tracked at slightly lower than estimated levels through August.

In the Sworn Recruitment and Training Program, 33 Officers that were part of the January 2003 Academy are currently in field training and are expected to be street-ready in October 2003.

GENERAL FUND (CONT'D.)

EXPENDITURES (CONT'D.)

KEY GENERAL FUND EXPENDITURES
(\$000's)

<u>Department</u>	<u>2002-2003 Budget</u>	<u>YTD Actual</u>
Police (Cont'd.)	\$ 217,776	\$ 29,029

Overtime expenditures through August were below expected levels at \$708,000 or 9.9% of the budgeted level (compared to the estimated level of 13.0%). In February 2003, the Department implemented guidelines on overtime usage. The Department continues to be proactive in managing overtime usage.

The compensatory time balance at the end of August is 212,106 hours for sworn personnel. This level represents a drop of 7,289 hours from the June 2003 balance of 219,395 hours, but an increase of 3,882 hours from the August 2002 balance of 208,224 hours.

<u>Department</u>	<u>2002-2003 Budget</u>	<u>YTD Actual</u>
Fire	\$ 109,767	\$ 14,863

Overall, expenditures for the Fire Department appear to be tracking approximately at budgeted levels. Efforts continue, however, to address paramedic staffing levels in the department. As of the end of August, the Department had a total of 206 filled front-line (125) and support (81) paramedics. As discussed during last year's budget process, this front-line total is still short of the 147 that are necessary to fully staff all apparatus. During last fiscal year, the Department implemented several strategies to close the gap in front-line paramedics. In March 2003, the accelerated accreditation program for 13 Firefighter Paramedics resulted in an increase in the number of front-line Paramedics. In addition, 16 individuals have completed a Paramedic Academy and are in the internship phase of their training. Those firefighters are expected to be accredited in December 2003, thus further increasing the number of front-line Paramedics to a projected level of 136. The Department will continue to work with the City Manager's Office on long-term solutions to completely fill front-line paramedic staffing needs.

Current estimates indicate that the Department's level of Non-personal/Equipment expenditures at year-end also should be within the budgeted level.

GENERAL FUND (CONT'D.)

CONTINGENCY RESERVE

Through August, the General Fund Contingency Reserve was at the 2003-2004 Adopted Budget level of \$25,086,675.

OTHER FUNDS

Construction and Conveyance Tax Funds

Continuing the positive trend experienced at the end of last fiscal year, collections through the first two months of the year were exceeding both prior year actuals and budgeted estimates. Through August, \$2.9 million in actual tax revenues had been received (17.8% of the 2003-2004 estimate of \$16 million). This collection level was 38.7% higher than revenues received through August 2002. In addition to these revenues, the City has since received September Conveyance Tax receipts which totaled \$3.0 million. This was 42.9% higher than the September 2002 amount of \$2.1 million. The 2003-2004 budgeted estimate, by contrast provided for a 36% decrease from the 2002-2003 collection level. The budgeted drop is significantly higher than originally anticipated because collections in 2002-2003 were well above expectations (\$4.8 million). While the news remains positive, we should continue to exercise caution when projecting year-end receipts. The prolonged economic downturn could still significantly impact housing sales, which are the primary drivers of this revenue.

Other Construction-Related Revenues

After an unexpectedly robust end to 2002-2003, construction-related activity began 2003-2004 with two slow months. The year-to-date total of the seven revenue sources monitored for this report is \$3.8 million, a decrease of 30.3% from the \$5.5 million collected through the same period last year, when August receipts were atypically strong. Fortunately, however, on an overall basis, this performance still exceeds modified budget estimates that allow for a 33.6% drop from the prior year.

The revenue picture is somewhat mixed across sources. The major revenue sources – Building and Structure Construction Taxes and Construction Excise Taxes – outperformed year-to-date estimates but tracked lower than in 2002-2003, due to the prior year's atypically strong August. Building and Structure Tax receipts through August totaled \$1.4 million (19.4% of the current 2003-2004 estimate of \$7,273,000), which represents a decrease of 28.9% from the revenues collected through the same period last year (\$2.0 million). It should be noted, however, that the budgeted estimate for this category allows for 32.4% drop in 2003-2004. Construction Excise Tax revenues through August totaled \$2.1 million (19.0% of the current 2003-2004 estimate of \$11 million), which represents a 34.1% decrease from last year's \$3.2 million received over the same period. The budgeted estimate for this category allows for a 35.1% drop in 2003-2004.

OTHER FUNDS (CONT'D.)

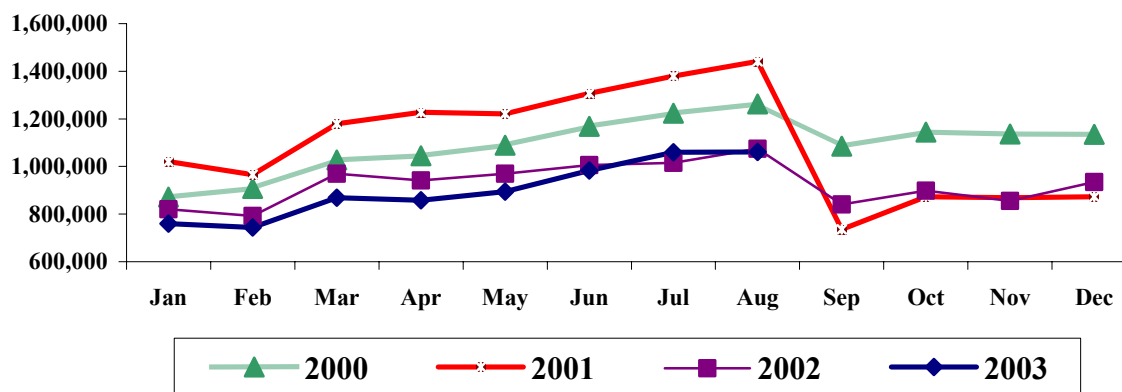
Other Construction-Related Revenues (Cont'd.)

Other construction related revenues are generated by Municipal Water Service Connection Fees, Sanitary Sewer Fees, Storm Drain Fees, Residential Construction Taxes, and Municipal Water Major Facilities Fees. All of these categories are tracking above prior year levels and at those collection levels would end the year at or above estimates, with one exception: Service Connection Fees. Receipts in this category through August totaled \$11,256 (only 3.4% of the current 2003-2004 estimate of \$325,000), compared to no receipts through August 2002. Because Service Connection Fee revenues recover actual costs to install new services, however, this low collection level should be coupled with lower costs.

Airport Funds

On a fiscal year-to-date basis, the Norman Y. Mineta San José International Airport (SJC) has enplaned and deplaned just over 2.1 million passengers, a slight increase of 1.5% from the figures reported through August of the prior year. However it should be noted that the growth was all due to increased July activity. Monthly passenger activity for August was down 1.2% from 2002. Passenger activity continues to be adversely impacted by such factors as the downturn in the local business and high-tech economy, as well as aviation industry-wide scheduling cutbacks. In August 2003, the Airport served 1.06 million passengers.

**Norman Y. Mineta San José International Airport
 Monthly Passengers**



Terminal C passenger activity for August 2003 increased 5.4% while year-to-date activity was up by 8.1%. Terminal C air carriers reporting reduced fiscal year passenger totals are Continental (down 14.8%), Northwest (down 13.5%), and United (down 9.6%). Those experiencing fiscal year passenger growth include Horizon (29.1%), Delta (13.1%), Mexicana (12.7%), America West (10.6%), Skywest (6.3%), and Alaska (1.9%). The advent of

OTHER FUNDS (CONT'D.)

Airport Funds (Cont'd.)

operations by American Trans Air has resulted in 45,248 additional passengers and the increase in activity from Frontier Airlines added 23,443 passengers flying out of Terminal C this fiscal year. Terminal A activity decreased 4.7% in August to August comparisons and is 2.0% lower than the figure reported through August 2002. Although American Eagle and Southwest reported increases in fiscal year activity of 613.8% and 6.6%, respectively, American Airlines decreased 23.9% from fiscal year 2002 activity.

Fiscal year-to-date mail, freight and cargo totaled 39 million pounds, which represents a 25.6% decrease from 2002-2003. The decrease is largely attributable to the termination of operations of Emery Worldwide Airlines and Kitty Hawk Air Cargo, although all cargo carriers showed reduced levels of activity in the current fiscal year: UPS down 15.5%; Air Trans down 14.4%; FedEx down 6.7%; and Airborne down 1%.

August 2003 taxicab operations decreased by 7.8% from those in August 2002, and are 4.3% lower than those recorded in 2002-2003. Year-to-date Passenger Facility Charge (PFC) revenues were 2.0% greater than the previous fiscal year.

Year-to-date operating revenues of \$12.6 million in the Airport Revenue Fund are 96.2% of budgeted levels. This performance is principally due to lower than anticipated revenues in terminal concessions and general and non-aviation programs. In terminal concessions, fewer rental car transactions have decreased revenue from rental car agencies operating at the Airport.

Early in September, the Mayor and City Council were notified by the Director of Aviation that with the 2002-2003 year-end close and audit, year-end financial results showed savings \$5.7 million greater than estimated. As a result, the Airport was able to reduce commercial aircraft landing fee by 11.0%, returning to the 2002 level of \$1.34 per thousand pounds of maximum gross landed weight. This fee rollback serves to support existing businesses, as well as promote SJC as a good place to bring in new business.

Through August, expenditures in the Airport Maintenance and Operations Fund are tracking below budgeted levels in both personal and non-personal/equipment categories. In personal services, expenditures totaled 12.3% of budget compared to a prorated benchmark of 13.0%. Savings are attributed to departmental vacancies and reduced overtime expenses. Through the end of August, the Airport carried 69 vacancies, of which 40 were funded. Of these vacant positions, 14 are funded in the Airport Capital Budget and do not impact personal services expenses in the Airport Maintenance and Operations Fund. Vacancy savings are partially offset by two pool employees and one overstrength position.

OTHER FUNDS (CONT'D.)

Airport Funds (Cont'd.)

Overtime expenditures to date total \$16,405 or 4.0% of budget, as compared to \$18,671 year-to-date in 2002-2003. Overtime at the Airport is used to provide critical holiday coverage, support after hours mandated staffing levels and provide emergency response. For the most part overtime (126 hours or 57.0% of total use) was directly related to staffing necessary to manage vehicle and pedestrian traffic in front of the terminals to insure the safety of our customers. Of the remaining 94 hours of paid and comp overtime reported, 32 hours were related to minimum level staffing of Badging Office, Airport Communication Center and weekend standby coverage provided for response to emergencies associated with the HVAC and electrical systems. The remaining hours were necessary for a network security project, airfield marking, emergency air conditioning repair and supervision. Paid overtime for Airport employees for August 2003 totaled \$5,279 as compared to \$7,941 paid in August 2002.

Non-personal/equipment expenditures through August total \$2.2 million, or 5.5% of the 2003-2004 non-personal/equipment budget. This performance contrasts with a prorated year-to-date expenditure benchmark of 8.4%. In particular, lower than estimated expenditures have been booked in contractual services where only 4.4% of the budget in this category has been expended. Current encumbrances amount to \$7.8 million, bringing total commitments to \$10.0 million or 25.0% of budget. At this time, however, non-personal/equipment savings recorded to date should be viewed as preliminary. Additional encumbrances are anticipated in the contractual services that could increase the rate of expenditure, bringing total expenses to benchmark levels. In addition, other details that show savings, such as overhead, will be fully expensed by year-end.

Year-to-date revenues from the Airport Customer Facilities and Transportation Fee Fund totals \$340,609 approximately 16.0% below anticipated budget levels due to reduced activity, and are 8.8% below the prior year levels. Current month expenditures of \$365,727 are 9.0% less than anticipated for August. Expenditures are tracking lower than anticipated due in large part to careful management and reduced bus operator, maintenance and fuel costs. Although it is too early to say whether expenditure reductions or additional revenue will be needed, this fund relies heavily on fees generated from business travelers. If activity does not rebound, further expenditure reductions or additional revenues may be required.

Transient Occupancy Tax Fund

Transient Occupancy Tax (TOT) collections of \$412,000 through August were \$130,000 below anticipated levels and down 5.0% from last year's same period. As described earlier, the August 2003 occupancy rate in the largest hotels of 53.2% was up slightly from the August 2002 rate of 53.1%, but below the July 2003 rate of 56.8%. In addition, while the number of rentable rooms remained stable over the prior year, the average room rate continued to slip, dropping to \$100.37 from \$120.05.

OTHER FUNDS (CONT'D.)

Transient Occupancy Tax Fund (Cont'd.)

Based on these trends, it would appear that collections in this fund will end the year well below the \$10.0 million budget. Staff will continue to monitor this fund closely and bring forward recommended adjustments if necessary as more information becomes available. The three recipients of the proceeds of this fund have been placed on notice that further reductions in their budgeted allocations will likely be necessary.

CONCLUSION

Economic indicators and City revenue collections confirms the fact that the City continues to be mired in an economic slowdown and will likely remain so for the immediate future. Since the Adopted Budget assumed this situation we believe that performance to date is consistent with budgeted estimates. We, of course, will need to closely monitor events and be ready to bring recommendations for any additional adjustments to either revenue or expenditure budgets to the City Council, as appropriate, through the Monthly Financial Report process and the Mid-year Budget Review.

Although the breadth and depth of the weak local economy has clearly been greater and longer than any of us anticipated, to date we have been able to weather the situation relatively well, largely due to the aggressive management measures implemented as soon as it became apparent that the economy had peaked. More tough decisions lie ahead. Based on early reports from the governor-elect, our \$55 million Motor Vehicle In-Lieu Fee revenue stream may be imperiled. This is in addition to the \$55 million+ shortfall already identified as likely in the General Fund in 2004-2005 as the result of local economic conditions. Planning is well under way within the Administration to develop options for how to address this situation. We do remain very confident, however, that our track record of prudent financial planning will continue to serve us well, and that working together we can and will respond appropriately.

As always, staff will continue to closely monitor our current year financial status and report regularly to the City Council on any significant developments through this reporting process.

LARRY D. LISENBEE
Budget Director